

# THE MAGIC CARE FORMULA

AEW UK FUND MANAGER IAN MASON REVEALS THE MAGIC FORMULA HE IS LOOKING FOR WHEN INVESTING IN A CARE HOME.

**C**HP: What are you looking for when making an investment?

**IM:** We are property investors so we are attracted very much to the property fundamentals. The key fundamental of everything we buy is focused on the occupier so where you have got demand higher than supply that's a very good dynamic. What is more important to us is the physical property and the fact that the care home has got a good place in the local environment and is serving a purpose and is well supported with good CQC ratings. It's very important to make sure that it's future proofed. One of the reasons that supply and demand is unbalanced is that CQC are quite rightly forcing up standards, which means a lot of converted, Victorian houses are falling out of the market.

Location is also important. We are looking for homes close to good transport networks for staff access. We shy away from the 'waiting for God' type homes in the country. It's important to bring senior living properties back into the town centre to help re-establish a sense of community and regenerate the local economy.

The thing that is most important to us is rent affordability. Southern Cross was the classic example where rents were set too high. Shocks came in terms of local authority funding rates being cut and debt costs were very high so that the revenue coming in was not enough to cover the rent and the



debt. You want to be working with an operator that is wary of that and doesn't want rent to become a real burden. We

want to know that if a company were to fail for other than demand reasons, would another company be willing to

come in and pay the same rent? Is the building of the right quality for another occupier? Can they afford to run the same sort of business as the existing operator so that they can afford to pay us the same rent?

**CHP: What makes sale and leaseback an attractive model?**

**IM:** Operators may want access to capital to fund their growth while keeping their home. A long lease guarantees they will continue to operate the home over the long term.

For our part we get access to a sector with very strong supply and demand fundamentals. If demand exceeds supply then rents should go up, all else being equal, and we have the comfort of knowing there is a long lease there. That's very important to some investors but less so to us. The lease on the Care UK home we acquired in Ascot had eroded to 19 years: too short for long lease funds that have to sell at 15 years, but that was in a good location with residential as an alternative use.

**CHP: How do you find your investments?**

**IM:** We tend to work with property advisers who are specialists in the sector. Knight Frank advised us on the Prime Life deals. The 'best' place for a lot of investors to target is the top five operators (such as Care UK) just because they are the biggest but not necessarily the strongest covenants.

What I learnt fairly early on is that it's actually the 'Division 2' players or small independents that have a reputation for providing better quality care. If you invest with them you are just as secure

if not more so as partnering with one of the big boys.

**CHP: Do you prefer private fee paying homes?**

**IM:** Care UK was a private fee paying model but if anything our homes leased to Prime Life are geared more towards the local authority market. We took the view that if their rents are affordable today after all the local authority cuts, which can't really be cut anymore and with the Living Wage having kicked in, and they are still profitable, then that is where we want to invest. The local authority model does not work in a number of places, however. When you look at some of the rates local authorities are providing, there is no way you can run a care home on those.

**CHP: Is the south east the most attractive region for you?**

**IM:** You can't afford to ignore the needs of the occupiers. Dementia is not something that only affects the south east. Our Prime Life homes are in Leicester. We are currently looking at homes in Doncaster and Darlington. We are going into areas where there is a very high demand for social needs.

**CHP: We have seen major hikes in private payer fees. Does that make the market more attractive?**


**IM:** Affordability has to start to impact on demand. It's dangerous to assume that local authority rates are going to be cut and cut, and private rates are going to go up and up. At some point affordability does start to impact even the most affluent. In the south east care home operators are having to compete more with alternative uses so that land prices are forced up. You then need to charge high fees in order to justify the price paid for the site. That's always a slightly dangerous model because you are hoping people are going to be able to afford to pay that. We heard of a

home in Brighton that had been opened up at £2,000 a week and the demand just wasn't there so they had to settle on £1,500. You can't assume you can charge what you want.

**CHP: How does your approach differ from Octopus and Target?**

**IM:** We need the operator to prove to us that the business is viable and they can afford to pay the rate. We will talk to them on a regular basis about how trade is going and what occupancy rates are and when they last refurbished their homes and the improvements they are going to be making to the home, but we let them get on with it. We are more hands off than the Octopuses and Targets of this world who are specialists who may be prepared to invest in homes that are at risk of failing. They can take on far more management risk. They have the contacts to be able to bring in new management to turnaround homes if they begin to fail. We want the rent and want to know that it is secure and capable of growing.

**CHP: Would you invest in Requires Improvement or Inadequate homes?**

**IM:** We would be if we thought the problem could be fixed and it was to do with the physical quality of the home. We would try and engage with the operator on the lease which might be a 30 year lease that has run down to five or 10 years. We could provide the funding to take their 'Grade B' home to 'Grade A', which would allow them to put their room rates back up and regenerate the business. In exchange we would want the right rent to extend the five-year lease back out to 25 years or 30 years. We understand the fundamentals of the sector. We buy Grade B office buildings and refurbish them so why is it such an amazing concept to do that with a care home as long as we can be rewarded for the risk? 

**AEW UK REAL RETURN FUND**

**Launch date:** Q1 2016  
**Net Asset Value:** £81.3m  
**Number of properties:** 34  
**Care home leaseholders:** Care UK, Prime Life